

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of Muskegon, Michigan conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to cities. GAAP includes all relevant Governmental Accounting Standards Board (GASB) pronouncements. In the government-wide financial statements and the fund financial statements for proprietary funds, Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, have been applied unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. For enterprise funds, GASB 20 and 34 provide the City the option of electing to apply FASB pronouncements issued after November 30, 1989. The City has elected not to apply those pronouncements. The more significant accounting policies establishing GAAP and used by the City are discussed below.

- Financial Reporting Entity - The City of Muskegon was incorporated October 6, 1919, under the provisions of the Home Rule Act of the State of Michigan. The City operates under a Commission-Manager form of government and provides the following services as authorized by its charter: general administrative services, public safety, highway and street maintenance, sanitation, culture, recreation and other governmental functions. As required by GASB 14, these financial statements present the City (the primary government) and its component units, entities for which the City is considered to be financially accountable. The component units discussed below are included in the City's reporting entity because of the significance of their operational or financial relationships with the City.
- Component Units - In conformity with generally accepted accounting principles, the financial statements of component units have been included in the financial reporting entity either as blended component units or as discretely presented component units. Each blended and discretely presented component unit has a December 31 year-end.
 - *Blended Component Units* - Blended component units, although legally separate entities, are, in substance, part of City operations and so data from these units are combined with data from the primary government.
 - City of Muskegon Building Authority - The Authority is governed by a three-member board comprised of the City Manager, City Attorney and City Finance Director. The City is involved in the purchase, by lease contract, of the City hall building and an automobile parking facility from the Authority. For financial reporting purposes, the Building Authority is reported as if it were part of the City's operations since its sole purpose is to acquire and lease property to the City.
 - *Discretely Presented Component Units* - The component units' columns in the government-wide financial statements include the financial data of the City's other component units. These units are reported in a separate column to emphasize that they are legally separate from the City.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- City of Muskegon Downtown Development Authority (DDA) - The Authority's sole purpose is the collection of tax increment revenues, the issuance and repayment of debt and the construction of public facilities to promote and facilitate economic growth in the downtown district. Members of the DDA are appointed by the City Commission and the Authority is fiscally dependent on the City since the City Commission approves the DDA budget and must approve any debt issuance.
 - City of Muskegon Local Development Finance Authority - The City has created three separate local development finance authority districts under the aegis of the Local Development Finance Authority (LDFA) to promote and facilitate economic growth in the Port City Industrial Park, the Medendorp Industrial Park, and the SmartZone Hi-Tech Park. The LDFA's sole purpose is the collection of tax increment revenues and the construction of public facilities. Members of the LDFA are appointed by the City Commission and the Authority is fiscally dependent on the City since the City Commission approves budgets and must approve any debt issuance.
 - Complete financial statements of the component units can be obtained from their administrative offices, 933 Terrace Street, Muskegon, Michigan 49443.
- *Related Organizations* - The following organizations are related to the City's financial reporting entity:
- Muskegon Hospital Finance Authority - The Muskegon Hospital Finance Authority was created by the City of Muskegon in accordance with the laws of the State of Michigan. Members of the Hospital Finance Authority are appointed by the City but the City is not financially accountable for the Authority and therefore the Authority is excluded from the accompanying financial statements. The Hospital Finance Authority's sole purpose is to issue tax-exempt debt for the benefit of Hackley and Mercy-General hospitals, both of which are located within the City. The Authority has no assets or financial activity and does not prepare financial statements. The Hospital Finance Authority has no taxing power. As of December 31, 2003, there was no outstanding debt issued by the Hospital Finance Authority. The City is not obligated in any manner for repayment of debt issued by the Hospital Finance Authority, as any debt is payable solely from contractual payments from the hospitals.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- Muskegon Housing Commission - The Muskegon Housing Commission was created by the City of Muskegon in accordance with the laws of the State of Michigan. Members of the Housing Commission are appointed by the City but the City is not financially accountable for the Commission and therefore the Commission is excluded from the accompanying financial statements. The Housing Commission's main purpose is to administer activities that provide adequate housing facilities for low-income families and the elimination of housing conditions that are detrimental to the public peace, health, safety and welfare. The Commission's policy is to prepare its financial statements on the basis prescribed by the Department of Housing and Urban Development. Accordingly, the summary information below (which is required by federal regulations), is not intended to present financial position and results of operations in conformity with generally accepted accounting principles. Summary financial information for the fiscal year ended September 30, 2003, the date of its latest audited financial statements is as follows:

Muskegon Housing Commission	
Total assets	\$5,455,749
Total liabilities	<u>222,942</u>
Total fund equity	<u>\$5,232,807</u>
Total operating income	\$286,485
Total operating expenditures	(2,047,621)
Total nonoperating revenues	<u>1,434,149</u>
Net loss	<u>(\$326,987)</u>

Complete audited financial statements can be obtained from the Muskegon Housing Commission at 1080 Terrace Street, Muskegon, Michigan 49442.

- *Joint Ventures* - The City of Muskegon participates in the following joint ventures:
 - Central Operations for Police Services - The City is a member of an area-wide central dispatch system, Central Operations for Police Services. It is a joint venture of nine governmental units governed by a board composed of representatives of the participants. It is financed through property taxes, an emergency telephone surcharge to the public and through annual member assessments based on population, composite state equalized valuation of property and the average of service calls placed. The City does not report an equity interest in this joint venture in these financial statements because the City does not have an explicit and measurable right to the joint venture's resources. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Financial information based on the September 30, 2003 audit report of Central Operations for Police Services follows:

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Central Operations for Police Services	
General Fund	
Total assets	\$1,554,240
Total liabilities	<u>136,581</u>
Fund balance	<u>\$1,417,659</u>
Revenues	\$3,052,078
Expenditures	<u>2,118,002</u>
Revenues over expenditures	<u>\$934,076</u>
General fixed assets account group	<u>\$ 2,080,810</u>
General long term debt	<u>\$ 393,448</u>

Complete financial statements for Central Operations for Police Services can be obtained from their administrative office at 860 Terrace St., Muskegon, Michigan 49443.

- Muskegon Regional Water Alliance - The City is a member of an area-wide alliance, the Muskegon Regional Water Alliance. It is a joint venture of seven governmental units governed by a board composed of representatives of the participants. It is financed through member assessments. The purpose of the alliance is to review, advise and participate in non-binding issues regarding water service within Muskegon County. The City does not report an equity interest in this joint venture in these financial statements because the City does not have an explicit and measurable right to the joint venture's resources. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Financial information based on the May 31, 2003 audit report of the Muskegon Regional Water Alliance follows:

Muskegon Regional Water Alliance	
General Fund	
Total assets	\$6,362
Total liabilities	<u>-</u>
Fund balance	<u>\$6,362</u>
Revenues	\$ -
Expenditures	<u>450</u>
Revenues under expenditures	<u>(\$ 450)</u>
General fixed assets account group	<u>\$ -</u>
General long term debt	<u>\$ -</u>

Complete financial statements for the Muskegon Regional Water Alliance can be obtained from their administrative office at 5428 East Apple Avenue, Muskegon, Michigan 49444.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- Basis of Accounting - Government-Wide Financial Statements - The statement of net assets and the statement of activities display information about the City as a whole. They include all funds of the reporting entity except for fiduciary funds. These statements distinguish between activities that are governmental and those that are considered business-type activities. Internal service fund activity is eliminated to avoid "doubling up" revenues and expenses.

The government-wide statements are prepared using the economic resources measurement focus and the accrual basis of accounting. This is the same approach used in preparation of the proprietary fund financial statements but differs from the manner in which the governmental fund financial statements are prepared. Therefore, governmental fund financial statements include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

The government-wide statement of activities presents a comparison between expenses, both direct and indirect, and program revenues for each segment of the business-type activities of the City and for each governmental and component unit program. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Some functions, such as administrative and financial services include expenses that are, in essence, indirect expenses of other functions. The City has elected not to allocate those indirect expenses to other functions. Program revenues include charges paid by the recipients of the goods or services offered by the programs and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues which are not classified as program revenues are presented as general revenues. The comparison of program revenues and expenses identifies the extent to which each program is self-financing or draws from the general revenues of the City.

Net assets should be reported as restricted when constraints placed on net asset use are either externally imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

- Basis of Accounting - Fund Financial Statements - Fund financial statements of the reporting entity are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues and expenditure/expenses. Funds are organized into three major categories: governmental, proprietary and fiduciary. The focus of governmental and enterprise fund financial statements is on major funds rather than reporting funds by type. A fund is considered major if it is the primary operating fund of the City or meets the following criteria:
- Total assets, liabilities, revenues or expenditures/expenses of that individual governmental or enterprise fund are at least 10 percent of the corresponding total for all funds of that category or type; and
 - Total assets, liabilities, revenues or expenditures/expenses of the individual governmental or enterprise fund are at least 5 percent of the corresponding total for all governmental and enterprise funds combined.

Each major fund is presented in a separate column. Non-major funds are aggregated and presented in a single column. The internal service funds are presented in a single column on the face of the proprietary fund statements. To improve reporting cohesiveness, the City has elected to include the Local Street and Marina funds as major funds for this report.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- The City reports the following major funds:
 - General Fund - The general fund is the general operating fund of the City. The fund is used to account for all financial transactions except those required to be accounted for in another fund. Revenues are derived primarily from property taxes, state shared revenues and charges for services.
 - Special Revenue Funds
 - Major Street and Trunkline Fund - To account for gas and weight tax allocations to the City by the Michigan Department of Transportation for construction and maintenance of major streets within the City.
 - Local Street Fund - To account for gas and weight tax allocations to the City by the Michigan Department of Transportation for construction and maintenance of local streets within the City.
 - Enterprise Funds
 - Water Fund - To account for user charges and for operating expenses and debt service of the City's water system.
 - Sewer Fund - To account for user charges and for operating expenses and debt service of the City's sewer system.
 - Marina Fund – To account for user fees collected and operating expenses for the Hartshorn Marina and boat launch ramp facilities.
- The following is a description of the three major categories and various fund types within those categories into which the funds are grouped:
 - Governmental Funds - All governmental funds are accounted for using modified accrual basis of accounting and the current financial resources measurement focus. Under the modified accrual basis of accounting, revenues are recognized in the accounting period in which they become susceptible to accrual (i.e., when they become both measurable and available). Expenditures are recognized in the accounting period in which the fund liability is incurred, if measurable.
 - ♦ Revenue Recognition - "Measurable" means the amount of the transaction can be determined and "available" means collectable within the current period or soon enough thereafter to be used to pay liabilities of the current period. The City considers income taxes, property taxes, special assessments, licenses, interest revenue and charges for sales and services as susceptible to accrual if the amount was due on or before fiscal year end and collection was within two months of year-end. Reimbursements due for expenditure-driven grants are accrued as revenue at the time the expenditures are made, or when received in advance, deferred until expenditures are made. All other revenue is recognized as payments are received.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- ◆ Expenditure Recognition - The measurement focus of governmental accounting is on decreases in net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related fund liability is incurred. However, principal and interest on general long-term debt, which has not matured, are recognized when paid. Allocation of costs, such as depreciation and amortization, are not recognized in the governmental funds.
- The following is a description of the governmental fund types of the City:
 - ◆ General Fund - The general fund is the general operating fund of the City. The fund is used to account for all financial transactions except those required to be accounted for in another fund. Revenues are derived primarily from property taxes, state shared revenues and charges for services.
 - ◆ Special Revenue Funds - Special revenue funds are used to account for the proceeds of specific revenue sources (other than special assessments and major capital projects) requiring separate accounting because of legal or regulatory provisions or administrative action.
 - ◆ Debt Service Funds - Debt service funds are used to record the funding and payment of principal, interest and related expenses in connection with certain long-term debt other than debt payable from the operations of the proprietary funds.
 - ◆ Capital Projects Funds - Capital projects funds are used to account for the acquisition or construction of major capital facilities other than those financed by proprietary fund operations.
 - ◆ Permanent Funds – The permanent funds are used to account for the assets of legal trust agreements held by the City as trustee for which only the interest income on the principal may be spent.
- Proprietary Funds - All proprietary funds are accounted for using the accrual basis of accounting. These funds account for operations that are primarily financed by user charges. The economic resource focus concerns determining costs as a means of maintaining the capital investment and management control. Their revenues are recognized when they are earned and their expenses are recognized when they are incurred. Allocations of costs, such as depreciation, are recorded in proprietary funds. Unbilled utility receivables are recorded at year end.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise funds and internal service funds are charges to customers for sales and services. The water and sewer funds also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses include the cost of sales and services, administrative costs and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- The following is a description of the proprietary fund types of the City:
 - ♦ Enterprise Funds - Enterprise funds report operations that provide services which are financed primarily by user charges, or activities where periodic measurement of net income is appropriate for capital maintenance, public policy, management control or other purposes.
 - ♦ Internal Service Funds - Internal service funds are used to record the financing of goods or services provided by the City to other departments and funds or to other governmental units on a cost reimbursement basis.
- Fiduciary Funds (Not Included in Government-Wide Financial Statements) - Fiduciary funds are used to report assets held in a trustee or agency capacity for others and therefore are not available to support City programs.
 - Agency Funds - Agency funds are used to account for assets held by the City in a trustee capacity or as an agent for individuals, private organizations, other governments and/or other funds. The agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.
 - Pension Trust Funds - The pension trust funds are used to account for the assets held by the City as trustee for the employee retirement systems.
- Budgets and Budgetary Accounting - Budgets are adopted on a basis consistent with generally accepted accounting principles. Annual appropriated budgets are legally adopted for the general and special revenue funds. The City adopts its budget in accordance with City Charter and Public Act 621, the Uniform Budgeting and Accounting Act, which mandates an annual budget process and an annual appropriation act to implement the budget. The City follows these procedures in establishing the budgetary data reflected in the financial statements:
 - Prior to September 1, the City Manager submits to the City Commission a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures and the means of financing them.
 - Public hearings are conducted at the City hall to obtain public comments.
 - Prior to September 25th the budget and annual appropriations act are legally adopted by the City Commission.
 - Formal budget integration is employed as a management control device during the year for all budgetary funds.
 - Budgetary control is exercised at the department level in the general fund, and at the total expenditure or "fund" level for the special revenue funds. Similarly, the City's "appropriation centers" are defined at the department level in the general fund and at the total expenditure or "fund" level for the special revenue funds. The City Manager is empowered to transfer line-item budget amounts within appropriation centers.
 - Budget transfers between appropriation centers or changes to appropriation center totals require formal amendment by the City Commission. Expenditures in the special revenue funds are classified by major functional category for informational purposes. Budgets for the current year are carefully reviewed throughout the year for any revisions of estimates. The legislative body amends the general appropriation act as soon as it becomes apparent this action is necessary. In 2003, the general fund and special revenue fund budgets were amended to reflect actual expenditures that were higher than originally budgeted.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- All budget appropriations lapse at the end of the year.
- Budgets as presented for the governmental funds are prepared on the modified accrual basis consistent with generally accepted accounting principles.
- Deposits and Investments - Statutes authorize the primary government and component units to invest in the following:
 - In bonds, securities and other obligations of the United States or agency or instrumentality of the United States.
 - In certificates of deposit, savings accounts, deposit accounts or depository receipts of a bank which is a member of the Federal Deposit Insurance Corporation, a savings and loan association which is a member of the Federal Savings and Loan Insurance Corporation or a credit union which is insured by the National Credit Union Administration.
 - In commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and which matures not more than 270 days after the date of purchase.
 - In United States government or federal agency obligation repurchase agreements.
 - In banker's acceptances of United States banks.
 - In obligations of this state or any of its political subdivisions that at the time of purchase are rated as investment grade by not less than one standard rating service.
 - In mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan.

The City's three pension trust funds are also authorized to invest in corporate bonds, common stock and certain other investment vehicles. The City's deposits and investments are in accordance with statutory authority.

The City maintains a cash and investment pool that is available for use by all funds and component units. Each fund type's or component unit's portion of this pool is displayed on the combined balance sheet as "cash and cash equivalents". In addition, certain City trust funds including the Policemen and Firemen Retirement Trust Fund, the General Employees Retirement Trust Fund and the Cemetery Perpetual Care Trust Fund have investments which are separately held from those of other City funds.

For the purpose of the statement of cash flows, the City considers all assets held in the cash and investment pool to be cash and cash equivalents because the investments are not identifiable to the specific funds and the assets can be withdrawn at any time, similar to a demand deposit account.

In accordance with State law, interest earned in the Budget Stabilization Fund is recorded in the General Fund.

Investments with a maturity of greater than one year at the date of purchase are stated at fair value, and all other investments are stated at cost or amortized cost.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- Receivables and Payables - Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “advances to/from other funds.” All other outstanding balances between funds are reported as “due to/due from other funds.” Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as “internal balances.”

All trade and property tax receivables are shown as net of allowance for uncollectible amounts. Property taxes attach as enforceable liens on property as of December 31st. Taxes are levied on December 1st of the following year and are payable from the date of levy through March 1st. Taxes levied on December 1st are recorded as receivables and deferred revenue. Taxes are recognized as revenue (and become available for appropriation) in the calendar year following the levy date (December 1st). The City bills and collects its own property taxes and also taxes for the county and school districts. Collections of all the taxes and remittance of them to the other taxing authorities are accounted for in the current tax fund. The City is permitted by state law without voter approval to levy taxes up to \$10.00 per \$1,000 of state equalized valuation for general governmental purposes, \$3.00 for sanitation, and up to \$50,000 per year for community promotion. The tax rate to finance City services for the year ended December 31, 2003, was \$10.0786 per \$1,000 of taxable valuation.

- Inventories and Prepaid Items - Inventories include materials, repair parts and supplies for various City operations and are valued at the lower of cost (first-in, first-out) or market. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.
- Restricted Cash and Cash Equivalents – Certain proceeds of the City’s enterprise fund revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants.
- Wastewater Facility Rights - The City is a participant in the Muskegon County Wastewater Management System, a wastewater treatment facility owned and operated by Muskegon County. Members are charged usage fees based on the volume of wastewater treated. In addition, each member municipality has pledged its full faith and credit in repayment of their allocated shares of long-term debt of the system. The City has a binding commitment from a large industrial user of the system to participate in the repayment of its share of the debt. The industrial user, whose demand for wastewater treatment accounts for 59% of the Citywide wastewater flow into the system, has agreed to fund 59% of the City’s share of the contracts payable to the County.

The City accounts for the group of transactions substantially in accordance with APB 17, Intangible Assets. The contract payable to Muskegon County is presented as long-term debt. The long-term receivable from the industrial user is recorded as an “other” asset and the difference, which represents the City’s investment in an intangible asset, is presented as wastewater facility rights. The investment in wastewater facility rights is amortized over the life of the debt issue.

- Capital Assets and Depreciation - Capital assets, which include property, plant, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$7,500 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost of purchase or construction. Contributed assets are recorded at estimated fair market value at the date of donation. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are also capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

	<u>Years</u>
Buildings	25 - 50
Improvements	40 - 50
Water and sewage mains	40 - 100
Equipment	5 - 20

- GASB 34 requires major networks and major subsystems of infrastructure acquired, donated, constructed or substantially rehabilitated since fiscal years ending after June 30, 1980 be inventoried and capitalized by the fourth anniversary of the mandated date of adoption of the other provisions of GASB 34. The City has capitalized infrastructure since January 1, 2002 when GASB 34 was implemented, and has reported the infrastructure in the statement of net assets. The City will retroactively capitalize the major infrastructure assets on or before December 31, 2007, as permitted by GASB 34.
- Compensated Absences - City employees are granted vacation and sick leave in varying amounts based on length of service and employee group. Unused vacation and sick leave days are paid to employees upon termination under limits that vary by employee group. The City follows the accounting and reporting principles outlined in GASB 16, with regard to employee vacation and sick leave. The liability for these compensated absences is recorded as long-term debt in the government-wide statements. The current portion of this debt is estimated based on historical trends. In the fund financial statements, a liability for these amounts is reported in the governmental funds only for employee terminations as of year-end while the proprietary funds report the liability as it is incurred.
- Long-Term Obligations - In the government-wide financial statements and the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.
- Cash Overdrafts - To facilitate cash management and to maximize interest income, the primary government and component units have pooled certain cash and investment accounts. Cash overdrafts represent a deficit position in the pooled account and have been classified as amounts due to other funds.
- Fund Equity – In the fund statements, reservations of fund balance represent amounts that are not available for appropriation or are legally segregated for a specific purpose. Reserves exist for prepaid expenditures and inventories as those items will be expended in subsequent years. Designations of fund balance represent tentative management plans that are subject to change.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

- Comparative Data - Comparative total data for the prior year have been presented in selected sections of the accompanying financial statements in order to provide an understanding of changes in the City's financial position and operations. However, comparative (i.e. presentation of prior year's totals by fund type) data has not been presented in each of the statements since its inclusion would make the statements unduly complex and difficult to read.

NOTE B - CASH AND INVESTMENTS

- Deposits - At year-end the carrying amount of the primary government and component unit's deposits was \$12,492,652 and the bank balance was \$12,272,761. Of the bank balance, \$100,000 was covered by federal depository insurance and \$12,172,761 was uninsured and uncollateralized.

Deposits are categorized below according to level of credit risk:

- Category 1 represents insured or collateralized deposits with securities held by the entity or by its agent in the entity's name.
- Category 2 represents collateralized deposits with securities held by the pledging financial institution's trust department or agent in the entity's name.
- Category 3 represents uncollateralized deposits including any bank balances that are collateralized with securities held by the pledging financial institutions, or by its trust department or agent but not in the entity's name.

	Category			Bank Balance	Carrying Amount
	<u>1</u>	<u>2</u>	<u>3</u>		
Demand Deposits	<u>\$100,000</u>	<u>\$ -</u>	<u>\$12,172,761</u>	<u>\$12,272,761</u>	<u>\$12,492,652</u>

- Investments - Investments of the primary government and component units are categorized below to give an indication of the level of risk assumed by the entity at year-end:

- Category 1 includes investments that are insured or registered, or for which the securities are held by the entity or its agent in the entity's name.
- Category 2 includes uninsured and unregistered investments, for which the securities are held by the counterparty's trust department or agent in the entity's name.
- Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in the entity's name.

	Category			Carrying Amount
	<u>1</u>	<u>2</u>	<u>3</u>	
US Government Securities	<u>\$6,824,653</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$6,824,653</u>
<u>Investments Not Subject to Categorization:</u>				
Stable Net Asset Value Money Market Mutual Funds				996,507
Variable Net Asset Value Equity/Bond Collective Funds				<u>86,437,579</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

\$94,258,739

NOTE B - CASH AND INVESTMENTS – Continued

Total deposits and investments at December 31, 2003, were \$106,751,391 and are presented in the fund financial statements as follows:

Balance Sheet Classification:	Combined Total
Governmental Funds Balance Sheet	
Cash and Cash Equivalents	\$5,630,443
Investments	6,824,653
Statement of Fund Net Assets – Proprietary Funds	
Enterprise Funds	
Cash and Cash Equivalents	3,646,033
Restricted Cash and Cash Equivalents	822,559
Internal Service Funds	
Cash and Cash Equivalents	2,050,882
Statement of Fiduciary Net Assets – Fiduciary Funds	
Cash and Cash Equivalents	5,156,212
Investments	81,694,610
Statement of Net Assets – Discretely Presented Component Units	
Cash and Cash Equivalents	925,999
	<u>\$106,751,391</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE C - CAPITAL ASSETS

- Primary Government - Capital asset activity for the year ended December 31, 2003 was as follows:

	Balance January 1, 2003	Additions	Deletions	Balance December 31, 2003
Governmental Activities				
Capital Assets Being Depreciated and Amortized				
Land Improvements	\$ 527,562	\$ 363,087	\$ -	\$890,649
Building and Other Improvements	14,559,534	581,093	-	15,140,627
Machinery and Equipment	10,638,577	554,461	434,835	10,758,203
Infrastructure	1,642,897	1,929,902	-	3,572,799
Shared Street Improvements	4,898,056	678,845	-	5,576,901
Total Capital Assets Being Depreciated and Amortized	32,266,626	4,107,388	434,835	35,939,179
Less Accumulated Depreciation and Amortization				
Land Improvements	131,252	20,924	-	152,176
Building and Other Improvements	10,319,345	597,695	-	10,917,040
Machinery and Equipment	7,802,551	892,701	426,488	8,268,764
Infrastructure	-	92,775	-	92,775
Shared Street Improvements	-	244,903	-	244,903
Total Accumulated Depreciation and Amortization	18,253,148	1,848,998	426,488	19,675,658
Net Capital Assets Being Depreciated and Amortized	14,013,478	2,258,390	8,347	16,263,521
Capital Assets Not Being Depreciated or Amortized				
Land	13,411,170	151,313	-	13,562,483
Construction in Progress	3,179,089	9,068,915	2,871,288	9,376,716
Total Capital Assets Not Being Depreciated or Amortized	16,590,259	9,220,228	2,871,288	22,939,199
Total Governmental Activities Capital Assets Net of Depreciation and Amortization	<u>\$30,603,737</u>	<u>\$11,478,618</u>	<u>\$2,879,635</u>	<u>\$39,202,720</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE C - CAPITAL ASSETS – Continued

	Balance January 1, 2003	Additions	Deletions	Balance December 31, 2003
Business-Type Activities				
Capital Assets Being Depreciated				
Land Improvements	\$ 1,925,473	\$ -	\$ 938	\$1,924,535
Buildings and Systems	49,607,809	1,094,691	141,257	50,561,243
Machinery and Equipment	3,061,746	-	1,484,979	1,576,767
Total Capital Assets Being Depreciated	54,595,028	1,094,691	1,627,174	54,062,545
Less Accumulated Depreciation				
Land Improvements	1,395,031	51,907	6,177	1,440,761
Buildings and Systems	19,224,006	803,168	18,668	20,008,506
Machinery and Equipment	1,449,106	85,041	768,374	765,773
Total Accumulated Depreciation	22,068,143	940,116	793,219	22,215,040
Net Capital Assets Being Depreciated	32,526,885	154,575	833,955	31,847,505
Capital Assets Not Being Depreciated				
Land	135,654	-	15,966	119,688
Construction in Progress	8,279,665	2,225,643	1,120,267	9,385,041
Total Capital Assets Not Being Depreciated	8,415,319	2,225,643	1,136,233	9,504,729
Total Business-Type Activities Capital Assets Net of Depreciation	<u>\$40,942,204</u>	<u>\$2,380,218</u>	<u>\$1,970,188</u>	<u>\$41,352,234</u>

➤ Depreciation was charged to programs of the primary government as follows:

Governmental activities	
Administrative services	\$448,635
Financial services	11,411
Public safety	103,803
Public works	37,546
Leisure services	207,865
Planning	19,057
Highways, streets and bridges	316,417
Internal service fund depreciation is charged to the various programs based on their usage of the assets	<u>704,264</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Total Governmental Activities	
Depreciation Expense	<u>\$1,848,998</u>
Business-type activities	
Water	\$282,302
Sewer	596,776
Marina	<u>61,308</u>
Total Business-Type Activities Depreciation Expense	<u>\$940,116</u>

NOTE C - CAPITAL ASSETS – Continued

- Discretely Presented Component Units – Capital asset activity for the City's discretely presented component units for the year ended December 31, 2003 was as follows:

	Balance January 1, 2003	Additions	Deletions	Balance December 31, 2003
Capital Assets Being Depreciated				
Buildings and Other Improvements	\$ -	\$3,798,258	\$ -	\$3,798,258
Less Accumulated Depreciation				
Buildings and Other Improvements	-	14,387	-	14,387
Net Capital Assets Being Depreciated	-	3,783,871	-	3,783,871
Capital Assets Not Being Depreciated				
Land	400,000	-	-	400,000
Construction in Progress	318,803	3,479,455	3,798,258	-
Total Capital Assets Not Being Depreciated	718,803	3,479,455	3,798,258	400,000
Total Discretely Presented Component Units Capital Assets Net of Depreciation	<u>\$718,803</u>	<u>\$7,263,326</u>	<u>\$3,798,258</u>	<u>\$4,183,871</u>

- Construction Commitments – As of December 31, 2003, the City and its component units had the following active construction projects and related commitments with contractors:

Project Name	Spent-to-Date	Remaining Commitment
Water Filtration Plant Improvements	\$552,286	\$16,847,714
Shoreline Drive East Construction	4,022,694	4,090,613
Cross Lake Ferry Site Improvements	-	1,200,000
Shoreline Drive Construction Engineering	654,511	413,434
Roberts Street Water Tank Painting	-	151,000
Public Service Building Heating Units	-	82,725

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE D - LONG-TERM DEBT

- Following is a summary of long-term debt transactions for the year ended December 31, 2003:

	Balance January 1, 2003	Borrowings	Payments	Balance December 31, 2003	Amounts Due Within One Year
<u>Business-Type Activities</u>					
Revenue Debt	\$9,750,000	\$ -	\$405,000	\$9,345,000	\$420,000
Intergovernmental Contractual Debt	7,038,014	-	1,151,091	5,886,923	1,107,267
Long-Term Compensated Absences	186,528	3,429	-	189,957	31,659
	<u>16,974,542</u>	<u>3,429</u>	<u>1,556,091</u>	<u>15,421,880</u>	<u>1,558,926</u>
<u>Governmental Activities</u>					
Intergovernmental Contractual Debt	1,276,900	-	150,000	1,126,900	150,000
Michigan Transportation Fund Debt	3,335,000	-	550,000	2,785,000	555,000
General Obligation Debt	400,000	-	195,000	205,000	205,000
Special Assessment Debt	1,835,000	1,575,000	375,000	3,035,000	425,000
Long-Term Compensated Absences	1,373,693	82,259	-	1,455,952	242,658
	<u>8,220,593</u>	<u>1,657,259</u>	<u>1,270,000</u>	<u>8,607,852</u>	<u>1,577,658</u>
Total Primary Government Long-Term Debt	<u>25,195,135</u>	<u>1,660,688</u>	<u>2,826,091</u>	<u>24,029,732</u>	<u>3,136,584</u>
<u>Discretely Presented Component Units</u>					
Revenue Debt	1,000,000	-	-	1,000,000	-
General Obligation Debt	9,390,000	-	995,000	8,395,000	180,000
	<u>10,390,000</u>	<u>-</u>	<u>995,000</u>	<u>9,395,000</u>	<u>180,000</u>
	<u>\$35,585,135</u>	<u>\$1,660,688</u>	<u>\$3,821,091</u>	<u>\$33,424,732</u>	<u>\$3,316,584</u>

- Long-term debt payable at December 31, 2003, consisted of the following individual issues:

Primary Government	
<u>Business-Type Activities</u>	
\$5,465,000 water supply system bonds of 1993 due in two installments of \$450,000 through May 1, 2013; interest at 4.50% (unamortized discount \$16,537).	\$ 900,000
\$9,575,000 water supply system bonds of 1999 due in annual installments of \$420,000 to \$800,000 through May 1, 2019; interest at 3.85% to 4.75% (unamortized discount \$77,117).	8,445,000
\$6,990,000 contractual obligation of 2002 for County wastewater debt due in annual installments of \$116,862 to \$1,244,580 through 2008; interest at 2.00% to 5.00%.	3,938,249

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Primary Government	
\$8,034,263 contractual obligation of 1996 for County wastewater debt retirement due in annual installments of \$964,112 to \$984,562 through July 1, 2005; interest at 5.10% to 5.70%.	<u>1,948,674</u>
Total Bonds and Loans Payable	15,231,923
Long-term compensated absences	<u>189,957</u>
Total Business-Type Activities Long-Term Liabilities	<u>\$15,421,880</u>

NOTE D - LONG-TERM DEBT - Continued

Governmental Activities

\$1,545,000 Building Authority limited tax bonds of 1996 (City Hall renovations) due in an annual installment of \$205,000 on December 1, 2004; interest at 4.30%.	\$205,000
\$1,155,000 special assessment improvement bonds of 1996 due in annual installments of \$25,000 to \$65,000 through December 1, 2005; interest at 4.30% to 4.40%.	90,000
\$1,495,000 special assessment improvement bonds of 1998 due in annual installments of \$60,000 to \$165,000 through April 1, 2009; interest at 3.90% to 4.00%.	780,000
\$825,000 special assessment improvement bonds of 2000 due in annual installments of \$70,000 to \$90,000 through April 1, 2010; interest at 4.55% to 5.00%.	590,000
\$1,575,000 capital improvement bonds of 2003 due in annual installments of \$105,000 to \$150,000 through June 1, 2016; interest at 2.00% to 4.05%.	1,575,000
\$1,276,900 State of Michigan urban land assembly loan due in annual installments of \$150,000 to \$276,900 through October 31, 2009; interest free.	1,126,900
\$2,245,000 Michigan Transportation Fund bonds of 2002 for street improvements due in annual installments of \$350,000 to \$400,000 through June 1, 2008; interest at 2.00% to 3.13% (unamortized premium \$7,119).	1,895,000
\$1,950,000 Michigan Transportation Fund bonds of 1998 for street improvements due in annual installments of \$205,000 to \$240,000 through December 1, 2007; interest at 4.10% to 4.25%.	<u>890,000</u>
Total Bonds and Loans Payable	7,151,900
Long-term compensated absences	<u>1,455,952</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

Total Governmental Activities Long-Term Liabilities	<u>\$8,607,852</u>
Total Primary Government Long-Term Debt	<u>\$24,029,732</u>

NOTE D - LONG-TERM DEBT - Continued

<u>Discretely Presented Component Units Debt</u>	
\$1,000,000 Downtown Development Authority promissory note to Muskegon County due in a balloon payment August 30, 2019; interest free.	\$1,000,000
\$4,005,000 Downtown Development Authority tax increment refunding bonds of 2001 due in annual installments of \$180,000 to \$335,000 through June 1, 2018; interest at 4.00% to 5.00%.	3,670,000
\$4,725,000 Local Development Finance Authority tax increment bonds of 2002 for building improvements in the Smartzone Tech Park due in annual installments of \$80,000 to \$400,000 through November 1, 2025; interest at 3.25% to 4.85% (unamortized discount \$8,597).	<u>4,725,000</u>
Total Discretely Presented Component Units Long-Term Debt	<u>\$9,395,000</u>
Total Reporting Entity Long-Term Debt	<u>\$33,424,732</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE D - LONG-TERM DEBT - Continued

- The annual requirements to amortize all debt outstanding as of December 31, 2003, including interest payments of \$9,989,180 are as follows:

Year Ending December 31	Business-Type Activities		Governmental Activities		Discretely Presented Component Units		Totals
	Principal	Interest	Principal	Interest	Principal	Interest	
2004	\$1,527,267	\$671,958	\$1,335,000	\$198,379	\$180,000	\$365,640	\$4,278,244
2005	1,515,974	600,244	1,115,000	158,123	185,000	358,340	3,932,681
2006	1,699,580	552,333	1,120,000	126,535	200,000	350,640	4,049,088
2007	1,702,894	471,373	1,170,000	93,966	280,000	342,640	4,060,873
2008	1,711,208	390,288	880,000	60,379	290,000	331,840	3,663,715
2009	510,000	308,850	536,900	43,685	300,000	320,220	2,019,655
2010	535,000	287,160	190,000	34,755	310,000	307,813	1,664,728
2011	555,000	263,993	120,000	28,805	320,000	294,605	1,582,403
2012	580,000	239,108	125,000	24,393	425,000	280,834	1,674,335
2013	605,000	212,620	130,000	19,610	500,000	262,268	1,729,498
2014	635,000	184,798	135,000	14,508	575,000	240,715	1,785,021
2015	665,000	155,381	145,000	8,975	605,000	215,435	1,794,791
2016	695,000	124,266	150,000	3,031	640,000	188,343	1,800,640
2017	730,000	91,310	-	-	670,000	159,088	1,650,398
2018	765,000	56,167	-	-	710,000	127,750	1,658,917
2019	800,000	19,000	-	-	1,395,000	103,063	2,317,063
2020	-	-	-	-	400,000	85,485	485,485
2021	-	-	-	-	255,000	67,085	322,085
2022	-	-	-	-	265,000	55,355	320,355
2023	-	-	-	-	280,000	43,165	323,165
2024	-	-	-	-	295,000	29,585	324,585
2025	-	-	-	-	315,000	15,278	330,278
	<u>\$15,231,923</u>	<u>\$4,628,849</u>	<u>\$7,151,900</u>	<u>\$815,144</u>	<u>\$9,395,000</u>	<u>\$4,545,187</u>	<u>\$41,768,003</u>

- Future debt service requirements (i.e. principal and interest) by type of debt are as follows:

	General Obligation Bonds		Revenue Bonds	
	General Long-Term Debt	Discretely Presented Component Units	Enterprise Funds	Discretely Presented Component Units
2004	\$213,816	\$545,640	\$821,880	\$ -
2005	-	543,340	820,204	-
2006	-	550,640	822,399	-
2007	-	622,640	818,667	-
2008	-	621,840	819,228	-
2009	-	620,220	818,850	-
2010	-	617,813	822,160	-
2011 - 2015	-	3,718,856	4,095,899	-
2016 - 2020	-	3,478,733	3,280,745	1,000,000
2021 - 2025	-	1,620,465	-	-
	<u>\$213,816</u>	<u>\$12,940,187</u>	<u>\$13,120,032</u>	<u>\$1,000,000</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE D - LONG-TERM DEBT - Continued

	<u>Intergovernmental</u>	<u>Special Assessment</u>	<u>Michigan Transportation Fund Bonds</u>
	Business- Type Activities	Governmental Activities	Governmental Activities
2004	\$1,377,345	\$150,000	\$532,239
2005	1,296,015	150,000	471,865
2006	1,429,514	150,000	433,175
2007	1,355,599	200,000	395,828
2008	1,282,267	200,000	344,285
2009	-	276,900	303,684
2010	-	-	224,755
2011 -2015	-	-	751,291
2016 -2020	-	-	153,034
2021 -2025	-	-	-
	<u>\$6,740,740</u>	<u>\$1,126,900</u>	<u>\$3,610,156</u>

- There are a number of limitations and restrictions contained in the various bond indentures. The City is in substantial compliance with all the significant provisions of the bond indentures.
- The limited full faith and credit of the City has been pledged for repayment of special assessments bonds.
- The \$4,725,000 Local Development Finance Authority (LDFA) tax increment bonds of 2002 are partially guaranteed by the Community Foundation for Muskegon County. If LDFA tax increment revenues are not sufficient to cover debt service costs in any year, the Foundation has agreed to pay one-half of such shortfall up to \$75,000 annually.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE E - RECEIVABLES, PAYABLES AND TRANSFERS WITHIN THE REPORTING ENTITY

➤ Receivables and payables consisted of the following at December 31, 2003:

Fund/Component Unit	Receivable	Fund/Component Unit	Payable
General	<u>\$1,036,348</u>	Current Tax	<u>\$1,036,348</u>
State Grants	<u>177,313</u>	Lakeshore Trail	<u>177,313</u>
Major Street and Trunkline	8,081,356	General	6,239,088
		Local Street	493,226
		Enterprise Community	4,281
		EC Micro Loan	32,993
		Rehab Loan Escrow	4,221
		HOME Rehabilitation	291,054
		Community Development Block Grant	235,344
		State Grants	595,801
		Marina	72,012
		Cemetery Perpetual Care	<u>113,336</u>
	<u>8,081,356</u>		<u>8,081,356</u>
Total Primary Government	<u>\$9,295,017</u>	Total Primary Government	<u>\$9,295,017</u>
		Component Unit – Local Development	
Primary Government - General	<u>177,304</u>	Finance Authority II	<u>177,304</u>
Total Reporting Entity	<u>\$9,472,321</u>	Total Reporting Entity	<u>\$9,472,321</u>

Property taxes are collected in a central current tax fund from where they are distributed to the various taxing jurisdictions - including the City and its component units. Amounts owed the City at December 31, 2003 are shown as interfund payables/receivables. The amount due to the state grants fund from the lakeshore trail fund is for a match on a grant. Other interfund payables/receivables consist entirely of temporary loans to cover cash shortfalls in a given fund.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE E - RECEIVABLES, PAYABLES AND TRANSFERS WITHIN THE REPORTING ENTITY – Continued

➤ Transfers consisted of the following for the year ended December 31, 2003:

Fund	Transfers Out	Fund	Transfers In
General	\$1,240,856	Local Street	\$870,000
		L.C. Walker Arena	210,000
		State Grants	10,856
		Public Improvement	150,000
	<u>1,240,856</u>		<u>1,240,856</u>
Budget Stabilization	500,000	General	566,282
Revolving Loan	5,000		
Cemetery Perpetual Care	61,282		
	<u>566,282</u>		<u>566,282</u>
Major Street and Trunkline	525,049	Local Street	500,000
		Sidewalk Improvement	25,049
	<u>525,049</u>		<u>525,049</u>
Local Street	64,169	Sidewalk Improvement	64,169
TIFA Debt Service	120,000	L.C. Walker Arena	120,000
General Employees Retirement System	289,603	General Insurance	1,179,938
Police and Firemen Retirement System	890,335		
	<u>1,179,938</u>		<u>1,179,938</u>
Lakeshore Trail	224,386	State Grants	224,386
Total Reporting Entity	<u>\$3,920,680</u>	Total Reporting Entity	<u>\$3,920,680</u>

Each year, the general fund transfers funds to the local and major street funds and to the public improvement fund to finance capital improvement projects. The general fund also provides an operating subsidy transfer to the L.C. Walker arena fund. Also on an annual basis, the City's pension funds transfer funds to the City's insurance fund to offset the cost of retiree healthcare benefits. Other transfers between funds are made to meet grant matching requirements or other operational needs.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE F - DEFINED BENEFIT PENSION PLANS

- The primary government maintains two separate single employer contributory pension plans - the General Employees Retirement System and the Policemen and Firemen Retirement System - which cover all active full-time employees of the City. The pension plans are maintained as pension trust funds and are included as part of the City's reporting entity. Staff costs associated with administering the plans are paid from the city's general fund. Contractual service costs for investment management and consulting, actuarial services, custodial services and similar items are paid from investment earnings of the funds. A stand alone financial report of the pension plans has not been issued.
- Plan Descriptions - The following schedule is derived from the respective actuarial reports and from City information and reflects accounting policies, membership and plan provisions and actuarial assumptions for the two pension plans as of December 31, 2002:

	General Employees	Policemen and Firemen
General Information:		
Authority	City Ordinance	City Ordinance
Basis of Accounting	Accrual	Accrual
Asset Valuation:		
Reporting	Fair Value	Fair Value
Actuarial Valuation	Four-Year Smoothed Market	Four-Year Smoothed Market
Valuation Date	December 31, 2002	December 31, 2002
Actuarial Cost Method	Individual Entry Age	Individual Entry Age
Amortization Method	Level Percent (Open)	Level Percent (Open)
Remaining Amortization Period	10 Years	10 Years
Non-government investments in excess of 5%	None	None
Membership And Plan Provisions:		
Members:		
Active Participants	171	127
Retirees and Beneficiaries Receiving Benefits	158	156
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	21	4
Member Contributions:		
First \$4,200 of Earnings	3.0%	6.0%
Excess of \$4,200 of Earnings	5.0%	6.0%

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE F - DEFINED BENEFIT PENSION PLANS - Continued

	General Employees	Policemen and Firemen
Normal Retirement Benefit:		
Retirement Age	55 - 60	53 - 55
Years of Service (Minimum)	5 - 30	10 - 25
Accrual (First \$4,200 final average compensation)	1.9% - 2.25%	2.5% - 2.6%
Final average compensation in excess of \$4,200	1.9% - 2.25%	2.5% - 2.6%
Maximum (% of final average compensation)	None	75%-80%
Years to Vest	5 - 10	10
Assumptions:		
Investment Earnings	8.0%	8.0%
Salary Increases	5.0% - 8.8%	5.0% - 8.0%
Investment and salary assumptions include inflation at 5.0%.		

- Basis of Accounting - The pension plans' financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period they are due. The City's contributions to the plans are recognized when due and the City has made a formal commitment to provide them. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.
- Funding Policy - The City is obligated by the state constitution to make annual contributions to each of its pension plans based on actuarially computed percentages of covered wages in amounts sufficient to cover the normal cost of benefits and amortize prior service liabilities over a period of future years. Actuarial assumptions used in determining the annual funding requirements are set by the boards of trustees of each system. During the year ended December 31, 2002, contributions were made to the plans in accordance with contribution requirements determined by actuarial valuations of the plans as of December 31, 2000, and were as follows:

	General Employees	Policemen and Firemen
Retirement Contributions – Members	\$325,527	\$ 410,413
Retirement Contributions – City	-	290,431
	<u>\$325,527</u>	<u>\$700,844</u>

- Benefits – Pension benefit levels are established through negotiation and contract with the City's various collective bargaining units. Benefit levels for non-represented employees are established by policy of the City Commission.
- Investments - Investments are reported at fair value which is determined using selected bases as follows: short-term investments are reported at cost which approximates fair value; securities traded on a national exchange are valued at the last reported sales price; investments that do not have established fair values are reported at estimated fair value; and, cash deposits are reported at carrying amount which reasonably estimates fair value. The following summarizes the carrying values of investments of the City's two pension plans at December 31, 2002:

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE F - DEFINED BENEFIT PENSION PLANS - Continued

	Cost	Fair Value
General Employees		
Bond index fund	\$12,001,488	\$13,660,138
Common stocks (collective funds)	15,439,230	15,929,148
Other instruments	<u>595,704</u>	<u>595,704</u>
	<u>\$28,036,422</u>	<u>\$30,184,990</u>
Policemen and Firemen		
Bond index fund	\$16,662,038	\$18,968,452
Common stocks (collective funds)	21,193,161	21,802,940
Other instruments	<u>320,729</u>	<u>320,729</u>
	<u>\$38,175,928</u>	<u>\$41,092,121</u>

- GASB 25 Required Information - Three-year trend information as required by GASB 25 is presented below. GASB 25 required supplementary information is presented after the Notes to the Financial Statements.

Three Year Trend Information				
Actuarial Valuation Dated December 31,	Fiscal Year Ended December 31,	Annual Pension Cost (APC)	Percentage Contributed	Net Pension Obligation
<u>General Employees</u>				
1998	2000	\$50,987	100.00%	0
1999	2001	-	-	0
2000	2002	-	-	0
<u>Policemen and Firemen</u>				
1998	2000	\$98,491	100.00%	0
1999	2001	96,549	100.00%	0
2000	2002	290,431	100.00%	0

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE G - OTHER POST EMPLOYMENT BENEFITS

- In addition to the pension benefits described in Note F, the City provides healthcare benefits to retirees receiving a City pension. As of December 31, 2003, 313 retirees or beneficiaries were eligible for post-employment health care benefits. Specific benefit provisions vary by employee group; however, in general, benefits for retirees under age 65 are the same as for regular employees while retirees over 65 receive a Medicare supplemental benefit. Since 1987, the City has had an actuarial valuation of its post employment healthcare obligation performed each year and has followed a program of prefunding the obligation in the same manner as it funds the pension obligation. During 2003, the City made contributions to the retiree healthcare program as follows:

	General Employees	Police and Firemen
Contribution	\$ 305,265	\$ 581,837
As a % of Payroll	4.4%	8.4%

As of December 31, 2002 the total unfunded actuarial accrued liability computed for the City's retiree health benefits was \$8,889,702.

NOTE H - EXCESS OF EXPENDITURES OVER APPROPRIATIONS IN BUDGETED FUNDS

- P.A. 621 of 1978, Section 18(1) as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated.
- During the year ended December 31, 2003, the City incurred expenditures in certain budgetary funds which were in excess of the amounts appropriated, as follows:

	Amended Budget	Actual Expenditures
Budget Stabilization Fund	\$400,000	\$500,000

- The budget overage in the budget stabilization fund resulted from the need to transfer at year-end additional operating funds to the general fund.
- All expenditures over appropriations have either been paid by available revenues, transfers from other funds or by reduction of the current fund balance.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE I - RISK MANAGEMENT

- The City purchases insurance, participates in public entity risk pools and is self-insured for the various risks associated with City operations. The City's risk financing activities are accounted for in the general insurance internal service fund. Significant risk management activities of the City are accounted for and disclosed below as required by GASB 10.
- The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City obtains its liability and property insurance coverage as a member of the Michigan Municipal Risk Management Authority (MMRMA), a public entity risk pool providing liability and property coverage to its participating members. The City pays an annual premium to MMRMA for liability insurance coverage. The MMRMA is self-sustaining through member premiums and provides, subject to certain deductibles, occurrence based coverage by internally insuring certain risks and reinsuring risks through commercial companies. A \$75,000 deductible is maintained to place the responsibility for small charges with the City. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years. Changes in the fund's claim liability amount in 2003 and 2002 were as follows:

	City General Liability	
	2003	2002
Claims Liability at January 1	\$119,422	\$245,152
Current Year Claims and Changes in Estimates	115,266	136,525
Claim Payments	<u>(113,859)</u>	<u>(262,255)</u>
Claims Liability at December 31	<u>\$120,829</u>	<u>\$119,422</u>

- The City manages workers' compensation risk by participating in the Michigan Municipal Workers' Compensation Self-Insurance Fund (MMWCSIF), a public risk pool providing workers' compensation coverage to its members. The City pays an annual premium to MMWCSIF for its workers compensation coverage. The MMWCSIF is self-sustaining through member premiums and provides statutory workers compensation coverage to its members by internally insuring certain risks and reinsuring risks through commercial companies. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.
- The City is self-insured for employee health care benefits for those employees selecting the City plan over other options. Under this plan, the general insurance fund provides coverage for up to a maximum of \$125,000 per covered individual. As of December 31, 2003, the claims liability including incurred but not reported claims was \$97,521. A liability was recorded in the accompanying financial statements for the estimated claims liability. The claims liability was based on past experience, a review of pending claims and other social and economic factors. The above estimate was not discounted and there were no outstanding claims for which annuity contracts have been purchased in the claimant's name. No significant reductions in insurance coverage were made in the last fiscal year. Settled claims have not exceeded the commercial coverage in any of the past three fiscal years. Changes in the fund's claim liability amount in 2003 and 2002 were as follows:

	City Employee Medical	
	2003	2002
Claims Liability at January 1	\$97,055	\$44,548
Current Year Claims and Changes in Estimates	1,527,828	1,520,235
Claim Payments	<u>(1,527,362)</u>	<u>(1,467,728)</u>
Claims Liability at December 31	<u>\$97,521</u>	<u>\$97,055</u>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE J - CONTINGENCIES

- The City has advanced funds in the amount of \$1,933,844 to the Downtown Development Authority (DDA) for activities involving redevelopment of the downtown area. Repayment of these advances is contingent upon collection of tax increment revenue (or "Proposal A" replacement revenues from the State) in excess of the amounts needed for debt service payments on outstanding bond issues. Repayment was uncertain and the advances were written off for financial statement purposes. If excess tax increment revenue (or "Proposal A" replacement revenues from the State) become available, the City will apply such revenue to repayment of the advances. The following advances were outstanding at December 31, 2003:

Date of Obligation	Original Amount	Outstanding Balance	Interest Rate
8/10/1989	\$1,150,000	\$1,150,000	0.0%
8/31/1989	783,844	662,032	7.0%

- The City is party to various other legal proceedings and claims which normally occur in governmental operations. Although the outcome of these legal proceedings and claims are not presently determinable, it is the opinion of the City's management that the resolution of these matters will not have a material adverse effect on the financial condition of the City.
- In the normal course of operations, the City receives grant funds from various federal and state agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

NOTE K - DESIGNATED FUND BALANCE

- Unreserved fund balances designated for specific purposes at December 31, 2003, are as follows:

Public Improvement Fund	
Designated for Fire Equipment Replacement	\$316,586
Designated for Pere Marquette Park Improvements	<u>5,982</u>
	<u>\$322,568</u>

NOTE L – SUBSEQUENT YEAR INFORMATION

- The City issued \$13,900,000 of water system revenue bonds through the Michigan Municipal Bond Authority to finance improvements at the water filtration plant. The bonds are dated March 25, 2004 and carry a fixed interest rate of 2.125%. The bonds are to be paid over twenty years with the first principal payment being made in 2006.

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003

NOTE M – SALE OF WATER SYSTEM

- During 2003, the City sold a part of its water system ("southside system") to Muskegon Charter Township. Ownership of the system and related issues had been the subject of litigation. Major terms of the sale are as follows:
- \$1,000,000 cash payment by the Township to the City in two equal annual installments in 2003 and 2004;
 - City agreed to waive hydrant rental fees in the amount of \$257,000 that had been in dispute;
 - Wholesale water sales by the City to the Township at a rate of 1.35 times the rate the City charges its residents;
 - The City to continue maintenance of the system under contractual arrangement; and
 - Township dismissed its lawsuit against the City.

At the time of sale, assets of the southside water system including receivables associated with hydrant rentals were carried on the City's books at a value of \$1,093,267. The sale price of \$1,000,000 resulted in a loss on the sale of \$93,267, which is shown in the water fund.

NOTE N – SUPPLEMENTAL INFORMATION TO STATEMENT OF CASHFLOWS

- A noncash transaction consisting of a payment due in the amount of \$500,000 for the sale of the southside water system to Muskegon Charter Township has been included in the accompanying water fund financial statements.

NOTE O – STATE CONSTRUCTION CODE ACT

- P.A. 245 of 1999, section 22(1) of the State Construction Code Act, requires fees generated by enforcing agencies of construction board of appeals be intended to bear a reasonable relationship to the actual cost of performing those services. The fees generated by the City's enforcing agencies and the costs of providing those services were as follows for the year ended December 31, 2003:

<hr/>	
Revenues	
Building permits	\$275,642
Plumbing permits	50,030
Mechanical permits	94,013
Electrical permits	125,718
Total Revenues	<hr/> \$545,403
Expenses	
Salaries and benefits	\$761,792
Supplies	18,780
Contractual services	152,279
Other expenses	14,710
Total Expenses	<hr/> \$947,561
Deficiency of revenues under expenses	<hr/> (\$402,158) <hr/>

City of Muskegon
NOTES TO FINANCIAL STATEMENTS
December 31, 2003